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IN THE

Supreme Court of the United States

October Term, 1963
No. 638

DAVID FARRELL and OLIVER J. FARRELL,
Petitioners,

vs.

UNITED STATES OF AMERICA,
Respondent.

Petition for Writ of Certiorari to Review a Decision of the U. S. Court of Appeals for the Ninth Circuit Affirming a Judgment of the U. S. District Court for the Southern District of California, Central Division.

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Petition for Writ of Certiorari to Review a Decision of the U. S. Court of Appeals for the Ninth Circuit Affirming a Judgment of the U. S. District Court for the Southern District of California, Central Division.

The petitioners above named respectfully petition and pray the Supreme Court to grant a writ of certiorari to review the judgment of the U. S. Court of Appeals for the Ninth Circuit dated August 7, 1963, 321 F. 2d 400 affirming a judgment of the U. S. District Court dated May 14, 1962. Copies of these judgments are appended hereto in chronological order.

I.

Statement of Grounds on Which the Jurisdiction of the Court Is Invoked.

The jurisdiction of the court is invoked upon the following grounds authorized by Rule 19, 1. (b) of the Rules of this Court:

1. That the Court of Appeals has decided an important question of federal law which has not been, but should be, settled by this Court and which decision also so far departs from the accepted and usual courses of judicial proceedings and has so far sanctioned such departure by the District Court wherein the petitioners have been deprived of their liberty without due process of law, contrary to the guarantee provided by the Fifth Amendment to the U. S. Constitution, all of which calls for the exercise of this Court's power and supervision.

2. The judgment of the Court of Appeals sought to be reviewed was dated August 7, 1963, and was entered on the same date.

3. On October 23, 1963, the Court of Appeals, by written opinion, denied the petition of petitioners for a rehearing which had been presented by petitioners herein. No order granting an extension of time within which to petition for certiorari has been requested or issued.

4. Jurisdiction in the Supreme Court to review the judgment in question by writ of certiorari is conferred by 28 U. S. C. A. 1254 (1).

II.

The Questions Presented for Review.

Were the petitioners, David Farrell and Oliver J. Farrell, denied due process of law and twice tried for the same offense in violation of the Fifth Amendment to the U. S. Constitution in the following particulars:

1. Petitioners were indicted, tried and convicted and sentenced to a multiple-count duplicitous indictment

when, in fact, only one crime, if any, was committed and only one sentence, if any, could be imposed.[1]

a. The indictment, conviction and sentence under the Corporation Securities Act of 1933 (15 U. S. C. 77 q (a) (1), a specific statute precluded an indictment, conviction and sentence under the general "mail fraud" statute (Title 18 U. S. C. §1341).

b. A charge of conspiracy to violate both the mail fraud and corporate securities act is duplitous and bad indictment in that it alleges a conspiracy to violate the general statute which is not a crime when the specific statute is charged.

2. The convictions under the allegations of violation of the Corporate Securities Act of 1933 are void in that the definition of securities as applied in the instant case is unconstitutionally vague.

a. As a matter of law, trust deeds secured by real property are not "securities" under the purview of the Corporate Securities Act.

b. As a matter of law, the petitioners could not have had the requisite, specific intent and knowledge that what they were selling was "securities" and the "conspiracy" conviction cannot stand.

3. As a matter of fact no "conspiracy" existed and the government's use of the conspiracy count was opprobrious, vexatious and an abuse of process.

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[1]The penalty provision relating to § 17 q (a) (1) may be found in 15 U. S. C. 77 x which provides, in pertinent part, as follows:

"Any person who willfully violates any of the provisions of this sub-chapter . . . shall, upon conviction be fined not more than $5,000.00 or imprisoned not more than 5 years or both."

4. The petitioners were subjected to irrelevant, immaterial and prejudicial introduction of testimony of the "victims" of the alleged fraud. In this connection, the court, having allowed the testimony of the alleged "victims" refused petitioners the right to introduce evidence.

III.

Constitutional Provisions and Statutes Which the Case Involves.

1. *U. S. Constitution.* The Fifth Amendment to the U. S. Constitution provides as follows:

> "No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use without just compensation."

2. 15 U. S. C. 77 q (a) (1), (§17 (a) (1) of the Securities Act), *re*: counts 1, 2, and 4 through 17, inclusive, provides in part as follows:

> "(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication and interstate commerce or by the use of the mails, directly or indirectly . . ."
>
> "(1) to employ any device, scheme or artifice to defraud . . ."

3. 18 U. S. C. 1341 (mail fraud statute) *re*: counts 18 through 32, inclusive, provides in part as follows:

> "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, . . . for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined not more than $1,000 or imprisoned not more than five years, or both."

4. 18 U. S. C. 371, which provides in part as follows:

> "If two or more persons conspire either to commit any offense against the United States, . . . and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both . . ."

IV.

Statement of the Case.

From late in 1957 to June 8, 1960,[2] the petitioners, Oliver J. Farrell and David Farrell, operated as officers of a corporation, a business engaged in the sale of discounted promissory notes secured by deeds of trust on real property located within the State of California. By virtue of the discounts, the public was assured of receiving earnings of ten per cent on the amount paid for the note and trust deed.

The gist of the "scheme to defraud" alleged by the government was in two parts:

> (1) That the promissory notes were "securities" as defined in §2 (1) of the Securities Act of 1933[3] and
>
> (2) That the notes sold were not processed or secured in the manner set forth in the brochures and sales talks used by the petitioners and the corporation, *i.e.*, some of the notes were secured by "raw" rather than "developed" land, and some of the investors did not receive their full ten per cent earnings, while others allegedly lost their en-

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[2]The date the receiver took over the business of L. A. T. D.

[3]"The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit—sharing agreement, collateral—trust certificate, reorganization certificate or subscription, transferable share, investment contract, voting—trust certificate, certificate of deposit for security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

§ 2(1) Securities Act of 1933; 15 U. S. C. 77b(1).

tire investment or did not receive their money back immediately after their demands for "liquidation" of their accounts (See App. 4).

The indictment filed on December 20, 1961 [C. T. 2-60], is in thirty-four counts. The first or "base" counts alleges a scheme to defraud a violation of §17 (a) (1) of the Security Act of 1933, 15 U. S. C. 77 q (a) (1). The next sixteen counts each allege a separate violation of the same act incorporating count one, the "base" count. The next sixteen counts also incorporated the "base" count, each describing the "scheme to defraud", but charging a general violation of 18 U. S. C., §1341 (mail fraud). The thirty-fourth count alleges a conspiracy (18 U S. C. 371) to violate both the Securities and the mail fraud acts and incorporates count one, constituting the elements of conspiracy. Two counts were dismissed by the government during the course of the trial [R. T. 3406].

Petitioners were arraigned under pleas of not guilty and following a twenty-seven day trial by jury, they were convicted on all thirty-two counts sent to the jury [C. T. 505-509]. A third defendant, Stanley C. Marks, was acquitted on all thirty-two counts [C. T. 512 (a)].

The petitioner, David Farrell, was sentenced on the sixteen securities counts to a cumulativ period of five years imprisonment and fined a total of $64,000.00. He was sentenced on the fifteen mail fraud counts to a cumulative period of five years imprisonment and fined a total of $15,000.00, the sentence of imprisonment to run concurrently with the sentence as imposed under the securities counts. He was also sentenced to five

years imprisonment on the conspiracy count and fined $7,500.00, with the prison sentence to run concurrently with the sentences imposed under the securities count and consecutively with the sentences under the mail fraud counts. Thus, David Farrell was sentenced to a total of ten years imprisonment and was fined a total of $86,500.00 [C. T. 554].

The petitioner, Oliver J. Farrell, was similarly sentenced to concurrent and consecutive terms of imprisonment, totaling four years, and fined a total of $50,000.00 [C. T. 554].

The jurisdiction of the District Court rests on §20 (b) and §22 (a) of the Securities Act of 1933, 15 U. S. C. 77 t (b) and 77 v (a) and 28 U. S. C. 1291 and 1294.

V.

Argument.

1. The Unlawful Indictment, Conviction and Sentence: 15 U. S. C. 77 q (a) (1), §17 (a) (1) of the Securities Act re: Counts 1, 2 and 4 Through 17, Inclusive, Provides That: "It Shall Be Unlawful for Any Person in the Offer and Sale of Any Securities . . . by the Use of the Mails, Directly or Indirectly, . . . to Employ Any Device, Scheme or Artifice to Defraud."

18 U. S. C. 1341, the mail fraud statute (counts 18 through 33, inclusive), provides in part that:

> "Whoever, having devised . . . any scheme or artifice to defraud . . . for the purpose of executing such scheme or artifice . . . or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department . . . (shall be fined and/or imprisoned)."

Both statutes, as can be seen from a glance, prohibit the same act. One, however, deals with the specific subject of securities. Since the allegations in the mail fraud count incorporate the allegations of count one, the "base count", it must show that the mail fraud convictions were obtained precisely on the same evidence with respect to the sale of securities.

It is familiar law that a specific statute controls over a general one, without regard to priority of enactment.

Bulova Watch Co. v. United States, 365 U. S. 753, 6 L. Ed. 2d 72, 81 S. Ct. 804;

Townsend v. Little, 109 U. S. 504, 512, 27 L. Ed. 1012, 3 S. Ct. 357.

Where the essence of a crime is a scheme to defraud and the use of the mails or other means of interstate commerce are incidental and merely for the purpose of providing federal jurisdiction, the individual transmissions do not constitute separate crimes.

United States v. Greenberg (D. C. N. Y. 1962), 30 F. R. D. 164.

From the above cited authorities, the conclusion must be reached that the judgment and conviction of violation of the general mail fraud statute cannot be sustained. Further, only one scheme to defraud was alleged so that the Corporate Securities Act and several convictions thereunder are therefore not permissible.

If the petitioners could not be charged with violating both the general and specific statutes of the conspiracy charge, alleging a conspiracy to violate both statutes must therefore be equally defective as duplicitous.

2. The Vague and Unconstitutional Statute.

This is a case of first impression in that it involves the unique prosecution for the sale of promissory notes secured by deeds of trust on real property situated within a single state. It was alleged by the government that the promissory notes were "securities" under the definition of §2 (1) of the Security Act of 1933 (See footnote No. 3, *supra*).

The case of *SEC v. Joiner*, 320 U. S. 344, 88 L. Ed. 88, enunciated the rule of construction for the Securities Act of 1933 holding, in a civil action, that the definition of securities was not so vague as to render it unconstitutional. Petitioners here submit that, as applied to petitioners, two important considerations compel either a reconsideration or a restatement of the Joiner Doctrine. First, in Joiner this court was not faced with a criminal conviction although the aspects of interpretation of criminal statutes was discussed in the opinion (320 U. S. 354, 355). Secondly, the petitioners herein were subjected to a complete trial and two Circuit Court opinions regarding the definition of "securities" before the criminal indictment was brought (see footnote No. 1, *supra*). In Joiner, the rule of the strict construction of penal statutes was again set forth with the modification that

> "the rule of strict construction was not violated by permitting the words of the statute to have their full meaning, or the more extended of two meanings, as the wider popular use instead of the more narrow, technical one; that the words should be taken in such a sense, bent neither one way nor the other, as will best manifest the legislative intent."

This Court emphasized that

> "we do nothing to the words of the Act; we merely accept them. It would be necessary in any case for any kind of relief to prove the documents being sold were securities under the Act. In some cases it might be done by proving the document itself, which on its face would be a note, a bond, or a share of stock. In other words, proof must go outside the instrument itself as we do here where this proof is offered in a civil action, as here, a preponderance of the evidence will establish a case; if it were offered in a criminal case, it would have to meet the stricter requirements of satisfying the jury beyond a reasonable doubt . . . ." (320 U. S. 355).

Prior to the criminal prosecution the government, the Circuit Court of Appeals (264 F. 2d 199) and the petitioners were either uncertain or in disagreement as to whether or not a second trust deed secured by California real property was in fact a "security" as defined in §2 (1) of the Securities Act.[4]

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[4] As pointed out in the body of the Petition, *infra*, the Circuit Court, in dealing with the first civil action wherein the receiver was set aside (264 F. 2d 199, 212), suggested that a proper determination of the case required a factual finding for a determination whether or not the petitioners were actually engaged in the sale of securities. Thereafter, when the factual determination was made contrary to the assertion of the petitioners the same Circuit Court in reviewing the evidence stated (285 F. 2d 162, 171-172):

> "The terms of the offer, the plan of distribution, the economic inducements held out to the prospects, the results dependent on one other than the purchaser, the common enterprise, *all combined herein to make the second trust deed notes 'securities'* as that term has been defined by the Supreme Court." (emphasis added) Citing, of course, *SEC v. Joiner*, 320 U. S. 344, and *SEC v. Howey*, 328 U. S. 293.

The stress on the words "all combined herein" by petitioners is to illustrate the problem a layman would have to guess whether or not he is within the purview of the Securities Act.

When the case came to the criminal jury after the judgment had been affirmed for the government in the civil case (285 F. 2d 162), the court was only able to give the jurors "guide lines" (see App. 3) for the determination of whether the notes were "securities" or "investment contracts" (see Paragraph 4, *infra*).

Petitioners submit that, where a course of conduct may or may not be criminal under federal law, depending on the definition of the word, the definition must be so exact that *external indicia* or the course of conduct itself cannot be the criteria for the determination of criminal liability. *SEC v. Joiner, supra*, to the contrary notwithstanding.

Assuming, as in Joiner, a looser definition of the word "securities" may be applied where civil sanctions are invoked under the Securities Act, it would be unconscionable to hold that a person may be held criminally liable for failing to guess correctly whether or not a court or jury will hold them to be bound by the Securities Act; especially as in the instant case where the petitioners were acting under advice of counsel and the Circuit Court (264 F. 2d 199) would not hold, as a matter of law, that the corporation was involved in the sales of securities.

"We suggest that a proper determination of this case requires an actual finding, in the court below

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Where men of average intelligence (with specific reference to lawyers in this instance) might reasonably differ in their interpretation of the combination of factors, certainly a layman can do no more than rely on the advice of counsel. Such a reliance must obviously be judicially declared to negate, under the circumstances, the criminal "knowledge" or "intent to support an indictment for violation of an offense where the heart of that offense revolves around the question of the definition of a word or the resolution of the combination of facts to define a word.

as to whether there was an investment 'in a common enterprise' and whether the purchaser 'is led to expect profit solely from the efforts of a promoter or a third party' [*SEC v. W. J. Howey Co.* (1946), 328 U.S. 293, 298-299, 66 S. Ct. 1100, 1103, 90 L. Ed. 1244] there must also be a consideration of the various other elements which cause or bar the recognition of a document, plan, course of dealing or program, as a security—all factors leading to the ultimate conclusion as to whether or not that which is here sold is subject to the Act" (264 F. 2d 212).

Compare this with the statement in the *Joiner* case, *supra*,

". . . instruments may be included within any of these definitions [of securities], *as a matter of law*, if on their face they answer to the name or description . . ." (320 U. S. 351, emphasis supplied).

Also, as pointed out, *infra*, under the law of the State of California where the land was situated, the promissory notes secured by the deeds of trust have been judicially declared *not to be the type of transaction which would subject their sales to the jurisdiction of the Securities Act.*

Consequently, the following conclusions can be reached: Either the statutory definitions as applied to these petitioners are unconstitutionally vague; or, as a matter of due process of law, a criminal conviction for violation of the Act (or conspiracy to violate the act) cannot be sustained because petitioners could not have had the requisite *mens rea, i.e.*, knowledge or intent for such a conviction.

Conspiracy is a specific intent felony. It imports a corrupt agreement between not less than two persons with a guilty knowledge on the part of each (*Morrison v. California*, 291 U. S. 82, 78 L. Ed. 664). In the instant case the petitioners had a bona fide dispute as to whether the Securities Act applied to their business, so the evidence could not be and was not sufficient to sustain any conviction for a conspiracy to violate the Securities Act.

Conversely, a conviction of conspiracy to violate the mail fraud statute cannot be sustained under the instant set of facts, since it cannot be ascertained from the record whether the conviction was for that conspiracy or the conspiracy to violate the Securities Act, or both.

Further, only one scheme to defraud was alleged so that the Corporate Securities Act and the several convictions and sentences thereunder are therefore not permissible.

United States v. Universal C.I.T., 344 U. S. 218, 97 L. Ed. 260, 73 S. Ct. 227.

3. As a Matter of Law, No "Conspiracy" Existed.

The shotgun approach to criminal prosecutions in the use of "conspiracy" allegations as in the instant case, is just that type of process condemned by this Court in *Krulewitch v. United States*, 336 U. S. 440, 69 S. Ct. 716, 93 L. Ed. 790 [concurring opinion]:

> "the unavailing protest of the Courts against the growing habit to indict for conspiracy in lieu of prosecuting for the substantive offense itself; or in addition thereto, against the loose practice as to this offense constitutes a serious threat to fairness in our administration of justice" (69 S. Ct. 719).

". . . As a practical matter, the accused often is confronted with a hodge podge of acts and statements by others which he may never have authorized or intended or even knew about, but which helped pursuade the jury of the existence of the conspiracy itself. In other words, conspiracy often is proved by evidence that is admissible only upon the assumption that the conspiracy existed on the naive assumption that the prejudicial effects can be overcome by instructions to the jury . . . all practicing lawyers know this to be unmitigated fiction" (69 S. Ct. 723).

If the petitioners herein were without actual knowledge that their acts were criminal or under the purview of the Securities and Exchange Commission, they could not have as a matter of law conspired to "commit any offense against the United States" (18 U. S. C. 371). They could have been at most principals, or aiders or abettors (*Pereira v. United States*, 347 U. S. 198, 198 L. Ed. 435, 74 S. Ct. 358). A fact of which the prosecution was well aware. It is submitted that it is about time this Court took judicial cognizance of the extensive and unprincipled use of the conspiracy statute by the Government in cases where such conspiracy charge is used merely to supplement the admission of otherwise inadmissible evidence and to sustain an extra conviction for an offense which in reality never existed.

If the conviction under the Securities Act cannot stand, neither can the conviction for an alleged "conspiracy" to violate that act.

Parr v. United States, 363 U. S. 370, 4 L. Ed. 2d 1277, 80 S. Ct. 1171.

4. As a Matter of Fact and Law, the Petitioners Were Not Engaged in the Sale of "Securities" as Defined by the Securities Act of 1933 and the Court's Instructions to the Jury Regarding Their Determination of This Fact Was Erroneous, Confusing and Prejudicial.

In reference to the securities counts, the Court instructed the jury that in order to sustain all or any one of these counts under the Securities Act, it was essential that the jury find not only that the defendants devised and engaged in a scheme to defraud by the use of the mails, as alleged in the indictment, but also the scheme to defraud involved the sale of securities as defined by the statute and alleged in the indictment (see App. 3).

The Court then instructed that Section 2 (1) of the Act defines the term "security" to include any note, evidence of indebtedness, investment contract, receipt for or guarantee of any such security. The Court further stated in its instruction (see App. 3):

> "getting back to the charges of the Securities Act, the requirement that the Government establish that the secured 10% earnings offered by the defendants involved the sale of securities will be established if you find that the trust deed notes or trust deeds are 'notes' or 'evidence of indebtedness' as defined by the Act.
>
> "Regardless of whether or not you find the trust deed notes or trust deeds are 'notes' or 'evidence of indebtedness' within the applicable statute, you may find the instrument should be classified as 'investment contracts' and therefore securities within the applicable statutes."

"The term 'investment contract' is not defined in the Act. There are, however, certain guide lines for you to follow in determining. . . .

"You need only find that the instruments here in question constituted securities under any one of the several definitions I have given you and not all of them or more than one of them."

(The petitioners' requested instruction and exceptions to the actual instruction are set out in App. 5). Petitioners contend that this instruction by the Court was erroneous in two respects:

First: The trust deed notes or trust deeds, in and of themselves, were not, as a matter of law, "notes" or "evidence of indebtedness" within the meaning of the Act;

Second: Neither "notes" nor "evidence of indebtedness" are defined by the Act and the Court gave the jury no definition or other guide by which to determine whether the trust deed notes or trust deeds were such "notes" or "evidence of indebtedness" as to make them securities within the meaning of the Act.

Petitioners' position is that the only charge should have been with regard to the type of security known as an "investment contract"; that the alternative given, wherein the jury could find the trust deed notes or trust deeds to be securities without the indicia of an "investment contract" was not only confusing and misleading but also an erroneous statement of law.

Those common law characteristics of a promissory note which might render it a "note" within the statutory definition of a "security", have been destroyed in California by various Legislative enactments with refer-

ence to purchase money deeds of trust. Under the successive amendments to Section 580(a), 580(b), 580(d), and Section 726 of the Code of Civil Procedure of the State of California, the maker of a purchase money deed of trust has no personal liability or obligation of any sort. The holder of the trust deed has no remedy or recourse against the maker. The trust deed becomes not an evidence of indebtedness but merely evidence of a charge or lien against the land. Where there is no debt as such, there can be no evidence of indebtedness. The cases of *Brown v. Jensen*, 41 Cal. 2d 193; *People v. Davenport*, 13 Cal. 2d 681, and *Nicholl v. Ipsen*, 130 Cal. App. 2d 452, support this interpretation of purchase money deeds of trusts in California. It is recognized that the decisions of State Courts would not be controlling with respect to the interpretation of a Federal statute (*L. A. Trust Deed & Mortgage Exchange v. SEC*, 264 F. 2d 199, 211). However, it is submitted that the Federal Courts are bound by the decisions of the highest Court of this State defining rights and liabilities under California law arising from a California contract or statute. If the California law declares that a promissory note, given in a purchase money transaction, should have none of the common law characteristics of a promissory note, the Federal Courts should not decree that it is still the common law "note" presumably intended by Congress when it classified a "note" as a "security".

Many of of the trust deeds finally evolved had no separate note at all [R. 2529-2530; Ex. 407 at P. 2292]. It would be absurd to classify a document as a security merely because one permissible form was used in lieu of another when, irrespective of whether

a note does or does not exist with the trust deed, it has the identical legal function, force and effect and is similar in all respects.

The same issue was before the Ninth Circuit Court in *L. A. Trust Deed & Mortgage Exchange v. SEC*, 264 F. 2d 199, and that Court specifically stated that it was not reaching the question as to the character of that which was sold. However, for the edification of the trial court, certain guide lines were set forth as follows (*ibid.*, p. 212):

> "We suggest that a proper determination of this case requires a factual finding, in the Court below, as to whether there was an investment 'in a common enterprise' and whether the purchaser is led to expect profits solely from the efforts of the promoter or a third party. [*Securities and Exchange Commission v. W. J. Howey Co.*, 1946, 328 U.S. 293, 298-299, 66 S. Ct. 1100, 1103, 90 L. Ed. 1244] There must also be a consideration of the various other elements which cause or bar the recognition of a document, plan, course of dealing or program, as a security—all factors leading to an ultimate conclusion as to whether or not that which is here sold is subject to the Act."

Such a mandate to the Court below, we submit, would not have been given if this Court had considered the second trust deed "notes" or "evidence of indebtedness" within the meaning of the Act.

Upon the conclusion of the trial the matter again came before the Ninth Circuit Court in *L. A. Trust Deed & Mortgage Exchange v. SEC*, 285 F. 2d 162. The first question raised was whether that which was

sold was a security within the Act. The SEC contended that the sale constituted more than a simple sale of second trust deeds—an interest in real property; that what was really involved was an investment contract (p. 166). The Court cited, discussed and relied upon two Supreme Court cases to guide it in solving the problems (*SEC v. C. M. Joiner Leasing Corp.*, 320 U. S. 344; *SEC v. W. J. Howey Co.*, 328 U. S. 293). With these guides in mind, and upon a review of evidence, the Court held that these petitioners—by their representations to the public, created and constituted the second trust deed notes securities subject to the Act (pp. 171-172). The Court concluded on this point as follows:

> "The terms of the offer, the plan of distribution, the economic inducements held out to the prospects, the results dependent on one other than the purchaser, the common enterprise, *all combine herein to make the second trust deed notes 'securities'* as that term has been defined by the Supreme Court" (emphasis added).

Implicit in this holding is recognition that the second trust deed notes, in and of themselves, were not securities. It was the overall activity in connection with the marketing of such instruments which combined to bring them within the reach of the Act. It was the presence of the indicia laid down in *Joiner* and *Howey* which made the second trust deed notes "securities".

The Court's charge to this jury on this basic issue was at best equivocal and constituted prejudicial error.

The jury was instructed that the sale of a "security" would be established if it found that the trust deed notes or trust deeds were "notes" or "evidences of in-

debtedness" as defined by the Act. No definitions were given and no guide lines were set forth to illuminate the meaning of "notes" or "evidences of indebtedness".

Although the Court instructed the jury at length on the tests to determine whether that which was sold was an "investment contract", and for that reason a security, the jury was left with a simple alternative requiring only a finding that a trust deed note was a "note". The adequacy of the instructions given on the tests for an "investment contract" is moot since the jury armed as it was with what was tantamount to an invitation to find the trust deeds to be "notes" under the Act, undoubtedly never reached the more involved decision posed by the "investment contract" issue. This seems more compelling in consideration that for some six weeks the jury heard the word "note" perhaps a thousand times.

The basic issue as to Counts One, Two and Four through Seventeen was whether or not that which was sold constituted a "security".

A conviction ought not to rest on an equivocal direction to the jury on a basic issue. Where there are erroneous instructions on a basic issue, a conviction cannot be sustained on some other theory even though the Appellate Court is left with no doubt that the defendant is guilty.

Hollenbach v. United States, 326 U. S. 607, 613;

Weiler v. United States, 323 U. S. 606, 611;

Yates v. United States, 354 U. S. 298, 327.

Cf.

Roe v. United States, 5th Cir. 1961, 287 F. 2d 435, 440.

where the Court said relative to an instruction which substantially instructed a verdict:

> ". . . No fact, not even an undisputed fact, may be determined by the Judge. The plea of not guilty puts all in issue, even the most patent truths. In our Federal system, the trial court may never instruct a verdict in whole or in part."

5. The Irrelevant, Immaterial, and Prejudicial Evidence and Testimony of "Victims" of the Alleged Scheme to Defraud.

The cases are legend that the success of the "scheme" is not essential to the completion of the offense of violation of either the Corporate Securities Act or the Mail Frauds Act (see note 52 United States Codes Annotated, Title 18, Section 1341):

> *Kreuter v. United States*, 218 F. 2d 532, certiorari denied, 75 S. Ct. 777, 349 U. S. 932, 99 L. Ed. 1262.

To be guilty of a crime of using mails to defraud, the defendant need not have actually obtained any money by his acts (*Erwin v. United States*, 242 F. 2d 336).

The Court committed error in allowing any testimony of losses by the customer-witnesses in that such evidence was (a) immaterial and irrelevant to the crimes alleged and (b) violative of the Court's own ruling in reference to events occurring after June 7, 1960 (the date the receiver took possession from petitioners).

The cutting edge of the Government's case was the selectivity with which the customers were chosen to testify and channels into which the adroit questioning led. The cutting effect of this edge was honed to a sharpness against which there was no effective defense.

(See discussion between counsel for petitioners and Government counsel and the Court and portions of the testimony, App. 4.) The sympathy effect on the jury of the testimony of Mr. Lees [R. 1806] who was 69 years of age, hard of hearing and unemployed; of Mr. Campbell [R. 1846-1847], who was 87 years of age and whose wife had to go to the County Hospital; of Mr. Schanz [R. 1820] who was 72 years of age, hard of hearing and obviously a man of no formal education; of Mrs. Hlavka [R. 1789] a widow; of Mrs. Eppley [R. 719] a 72 year old widow, was overwhelming. It was calculated to be.

Neither allegations nor proof of losses or that any one was actually defrauded was required. *Bobbroff v. United States* (9th Cir.), 202 F. 2d 389; see also *Hermansen v. United States* (5th Cir., 1956), 230 F. 2d 173. If such testimony was unnecessary it was therefore immaterial; why then did the Government try to prove the unnecessary? The only answer is that it was calculated to engender sympathy for the alleged victims and conversely antipathy against the defendants whose guilt or innocence the jury was soon to be called upon to judge.

It will be argued that petitioners' counsel by failing to object waived the objection and perhaps it is well taken. But perhaps the petitioners' attorneys were impaled on the horns of the dilemma noted and severely criticized by Judge Frank in 155 F. 2d 631, *infra*.

However, were this the only ploy used by the Government the severity of the error would not be so compelling. But, coupled with the finale scheduled for each witness' testimony as to not getting his money back, the net effect was overwhelmingly prejudicial. There was

a further ground upon which evidence of losses were inadmissible. This arose out of the fact a receiver took over a going business and the defendants had no control of events thereafter. The Court, as pointed out above, attempted to establish the date of take over by receiver as an effective barrier beyond which neither the Government nor the defendants would go. Admittedly, much evidence of events that occurred after the receiver was rejected.

However, on evidence of customer losses, this salutary barrier simply did not exist for the Government and it was free to roam on up to as late as the very day that the witness was testifying almost two years beyond the cutoff date. At the same time petitioners were effectively blocked in their pursuit of such evidence in order to rebut it. This was the source of constant objection and discussion with the Court as seen above (App. 4).

There can be no doubt of the validity of petitioners' position on the need for an effective cutoff date. However, the administration and application of the rule, as applied on evidence of losses, was manifestly unfair. The maximum latitude that can be said to be allowed to the prosecution in this case would be to inquire *if* the customer had *tried before June 8, 1960* to convert his position to cash and if he had, what happened? The Court, on one occasion, suggested this as representative of its ruling but it was observed only in the breach by the prosecution.

Cf. Lockhart v. United States (9th Cir., 1929), 35 F. 2d 905, citing with favor *Waldron v. Waldron*, 156 U. S. 361, 15 S. Ct. 383, 39 L. Ed. 453. See also the dissenting opinion of Judge Frank in *United States*

v. Antonelli Fireworks Co. (2nd Cir., 1946), 155 F. 2d 631, for an exhaustive treatise on the subject of prejudicial misconduct and error. See also Judge Frank's concurring opinion in the *Grayson* case, *supra*. *Cf. Kotteakos v. United States*, 328 U. S. 750, 66 S. Ct. 1239, 90 L. Ed. 1557; *Bihn v. United States*, 328 U. S. 633, 66 S. Ct. 1172, 90 L. Ed. 1485; see also *Bollenbach v. United States*, 326 U. S. 607, 66 S. Ct. 402, 90 L. Ed. 350; *Weiler v. United States*, 323 U. S. 606, 65 S. Ct. 548, 89 L. Ed. 495, 156 A. L. R. 496; *Bruno v. United States*, 308 U. S. 287, 293, 60 S. Ct. 198, 84 L. Ed. 257.

In summary, it is submitted that the errors complained of were prejudicial and constitute sufficient grounds standing alone to warrant reversal. Obviously the error was not corrected by the Court's instruction; nor could any instruction have cured the error already created in the jury's mind. Furthermore the error when taken in conjunction with the other errors assigned, make it clear petitioners did not receive that which they deserved—a fair trial.

As is pointed out in Appendix 4, *supra*, the existence of such "victims" was a matter completely beyond the control of the petitioners in view of the take over by the receiver on June 8, 1960. The petitioners were not allowed to present to the jury the fact that the receiver held funds for the purpose of liquidating the customers account since the petitioners were prevented from going into any matter, fact or happening occurring after June 8, 1960, even though the "victim" witnesses were allowed to answer the questions of the Government concerning matters as of the date of the trial. This was tantamount to a willful suppression of the evidence by

the Government. On the foregoing the unalterable conclusion must be reached that the staging of the select witnesses by the Government and the introduction of such irrelevant and immaterial evidence was purposefully done with the intention of creating bias, prejudice, and passion in the minds of the jurors with the full knowledge that at the time such evidence was presented, the defendants were in the impossible position of being unable to refute the *innuendo* that the monies paid to the corporation for the purchase of trust deeds was irretrievably lost to the customer-witnesses.

VI.

Conclusion.

The within Petition for Certiorari contains many important points of law concerning the interpretation of the Corporate Securities Act and of the mail fraud statutes which have not been precisely decided by this Court and a resolution of these problems is necessary and proper for the benefit of all persons similarly situated and for the guidance of the government and the courts below.

Wherefore, petitioners pray that this Court grant a Writ of Certiorari to review the judgment of the U. S. Court of Appeals for the Ninth Circuit dated August 7, 1963, 321 F. 2d 409, affirming the judgment of the U. S. District Court for the Southern District of California, dated May 14, 1962.

Respectfully submitted.

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APPENDIX I.

Opinion of the United States Court of Appeals for the Ninth Circuit.

United States Court of Appeals for the Ninth Circuit.

David Farrell and Oliver J. Farrell, Appellants, vs. United States of America, Appellee. No. 18,241. Aug. 7, 1963.

On Appeal from the United States District Court for the Southern District of California, Central Division.

Before: Jertberg and Browning, Circuit Judges, and Burke, District Judge.

Jertberg, Circuit Judge:

Following trial to a jury, the appellants David Farrell and Oliver J. Farrell, brothers, were convicted on thirty-two counts of a thirty-four count indictment. Upon the close of the government's case, the District Court dismissed Counts 3 and 33 on motion of the government.

Counts 1, 2, and 4 through 17, inclusive, [16 counts] charge offenses under Section 17 (a) (1) of the Securities Act of 1933 (15 U.S.C. 77q (a) (1)), which in pertinent part provides:

> "(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—
>
> "(1) to employ any device, scheme or artifice to defraud . . . ."

Counts 18 through 32, inclusive, [16 counts] charge offenses under the Mail Fraud Statute (18 U.S.C. 1341), which in pertinent part provides:

> "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, . . . for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined not more than $1,000 or imprisoned not more than five years, or both."

Count 34 charges a conspiracy to violate the Securities Act and the Mail Fraud Statute in violation of 18 U.S.C. 371, which in pertinent part provides:

> "If two or more persons conspire either to commit any offense against the United States, . . . and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both. . . ."

The first count alleges that appellants and one Stanley C. Marks [acquitted by jury verdict on all counts], devised a scheme to defraud investors in the sale of securities [investment contracts, promissory notes, and

evidence of indebtedness] issued by Trust Deed Mortgage Exchange (TD&ME), a California corporation, Los Angeles Trust Deed and Mortgage Exchange (LATD&ME), a California corporation, Trust Deed and Mortgage Markets (TD&MM) a California corporation, and Colorado Trust Deed and Mortgage Markets (CTD&MM), a Colorado corporation, in connection with an investment plan or program designated by appellants as a secured 10% earnings program, secured 10% earnings reinvestment program and secured 10% earning accounts, based on the sale to investors of discounted trust deeds and mortgages covering units of real estate situated within the State of California. The first count describes the scheme to defraud in detail.

Counts 2, and 4 to 17 inclusive, allege a separate violation of the quoted section of the Securities Act and incorporate by reference the allegations made in Count 1.

Counts 18 to 32, inclusive, incorporate the statement of the scheme to defraud as set forth in Count 1, except that the instruments through which the scheme was accomplished are not described as securities.

The 34th Count alleges and incorporates by reference the allegations made in Count 1 as constituting elements of conspiracy, and sets forth numerous other overt acts accomplished in furtherance of the conspiracy.

The case comes before us on a large record. The trial consumed over 27 trial days; over 2000 documents were received in evidence, and the reporter's transcript of testimony exceeds 4400 pages.

The appellant, David Farrell, did not specify as error, nor does he assert as error, the insufficiency of the

evidence to sustain the jury verdicts returned against him "simply in recognition of the limited role a reviewing Court has in such a situation." [Opening Brief, p. 13.] In this connection this appellant states: "While it is true it cannot be said as a matter of law there was no evidence nor inference drawable therefrom supporting the verdict, the evidence was weak and attenuated on the one real issue involved in the whole long trial—intent." [ibid. pp. 13-14.] Furthermore this appellant states: "Actually the trial of this case was remarkable in several ways, the most noteworthy of such is the astouding fact that there really is not much conflict as to the evidence. The operations and activities of TD&ME, LATD&ME and appellant from January, 1958 to June 8, 1960 and what was or was not said and done were really basically agreed to. An agreement, however, which carries with it no concession that a scheme or conspiracy to defraud ever actually existed. The few areas of dispute and how, if at all, these areas were resolved by the jury is not really opened to review." [ibid. p. 10.] This appellant's assignment of errors is as follows:

> "I. The Court erred in its instruction on the issue of security under The Security Act of 1933 on Counts One, Two, Four through Seventeen.
>
> "II. The Court erred in allowing introduction of any evidence of the existence of the prior civil act or the issues involved therein and its determination. There was also error in the phrasing of the Court summary and in the Court's failing to instruct at that time the difference between the burdens of proof in the two actions.

"III. The Court erred in allowing any testimony of losses by customer witnesses in that such evidence was (a) immaterial and irrelevant to the crimes alleged and (b) violative of the Court's own ruling in reference to events occurring after June 7, 1960.

"IV. The Court erred in admitting Exhibit 6003 in evidence."

The appellant, Oliver J. Farrell, adopts the assignment of errors made by his co-appellant, and in addition assigns as error solely on his own behalf, insufficiency of the evidence "on all counts as a matter of law to sustain the judgment of conviction on all counts." This appellant concedes that "in the prosecution of this case the government presented an extremely thorough case, establishing how the Los Angeles Trust Deed and Mortgage Exchange had engaged in a course of conduct which violated the Securities Act of 1933 and engaged in Mail Fraud."

We will first consider the separate assignment of error of the appellant, Oliver J. Farrell, whose basic contention under this assignment is "that the evidence is insufficient to impute to him any knowledge of any fraudulent scheme or any intent to defraud. His role as only sales manager in this highly departmentalized operation is thoroughly demonstrated throughout the record, as is the fact that David Farrell made all of the policy decisions, directed the operations of the company, and caused huge profits to be made by his solely owned, corporations which dealt with LATD&ME." [Opening Brief, p. 12.]

Thus, there is presented to us a narrow issue under this assignment.

The record discloses that this appellant was vice-president, secretary, a director and the sales manager of LATD&ME from the inception of the Secured 10% Earnings Program in late 1957 until June 1, 1960. He was also vice-president and a director of TD&MM. His compensation as sales manager for that period exceeded $250,000.00. As sales manager he employed, trained and supervised all local LATD&ME salesmen, and conducted weekly meetings throughout California, instructing salesmen in effective sales techniques. All branch managers took their orders from him and were directly responsible to him. He edited literature that was mailed out to investors. He furnished to investors false and misleading information concerning the liquidation policy of LATD&ME. He instructed the regional sales managers that the salesmen, in selling the 10% Earnings Programs, should resort to sham references in reassuring investors that their investments could be quickly liquidated. He assisted in drafting brochures sent to salesmen and investors which falsely represented the value and stability of subordinate trust deeds that were created against undeveloped subdivisions or vacant tracts of land. He instructed salesmen to represent that funds of LATD&ME were being used to purchase trust deeds for inventory, whereas, the funds of investors were being used for that purpose. He instructed salesmen to "play down" the issues and scope of litigation hereafter mentioned, initiated by the Securities & Exchange Commission against him, the corporations above mentioned, his co-appellant and others. He had some knowledge that his co-appellant enjoyed profits under some participation agreements with subdividers on land on which investors purchased sub-

ordinated trust deeds. He instructed salesmen to represent to investors that the subdividers who created trust deeds for LATD&ME against vacant tracts of land had made large cash investments in the subdivision, whereas, in some instances no investment had been made by the subdivider.

From the foregoing summary, and other evidence in the record which we have not mentioned, and upon inferences which might reasonably be drawn therefrom, the jury, by verdicts returned against the appellant, impliedly found, and concluded that appellant had knowledge of and participated in a course of conduct which violated the statutes upon which the indictment is based.

The decisions reveal two tests which are applied in determining the sufficiency of either direct or circumstantial evidence to support a jury verdict. The verdict of a jury must be sustained if there is substantial evidence when viewed in the light most favorable to support the judgment. *Glasser v. United States*, 315 U.S. 60 (1942); *Williams v. United States*, 273 F.2d 781 (9th Cir. 1959), C.D. 362 U.S. 951; *Robinson v. United States*, 262 F.2d 645 (9th Cir. 1959); *Miller v. United States*, 302 F.2d 659 (9th Cir. 1962). The verdict of a jury must be sustained if reasonable minds as triers of the fact, could find that the evidence excludes every reasonable hypothesis but that of guilt. *Remmer v. United States*, 205 F.2d 277 (9th Cir. 1953). See also: *Bolen v. United States*, 303 F.2d 870 (9th Cir. 1962).

Under either test, and bearing in mind that the credibility of witnesses and the weight to be accorded their testimony is peculiarly within the province of the trier

of facts, we conclude from our review of the record that the evidence is sufficient to sustain the jury verdicts returned against this appellant.

We will now consider ad seriatim the assignment of errors made by appellant, David Farrell, and adopted by the appellant, Oliver J. Farrell.

The first assignment:

> "1. The Court erred in its instruction on the issue of security under The Security Act of 1933 on Counts One, Two, Four through Seventeen."

The Court instructed the jury that each of the above mentioned counts of the indictment charges that the appellants:

> "devised and executed a scheme to defraud in the sale of 'securities' as defined in Section 2(1) of the Securities Act of 1933 namely, 'investment contracts, promissory notes, evidence of indebtedness and receipts for and guarantees of such securities,' in connection with an investment plan, program and arrangement designated by the defendants as a Secured 10% Earnings Program, Secured 10% Earnings Reinvestment Program, Secured 10% Earnings Accounts, and other similar designations, based on the sale to members of the investing public or discounted trust deeds and mortgages, in violation of Section 17(a)(1) of the Act, making it unlawful 'for any person to offer for sale any securities, by the use of any means or instruments of transportation or communication in interstate commerce, or by use of the mails, directly or indirectly, to employ any device, scheme or artifice to defraud.'"

The Court then instructed the jury that in order to sustain all or any one of such counts, it was essential that the jury find "not only that the defendants devised and engaged in a scheme to defraud by use of the mails, as alleged in the indictment, but also that the scheme to defraud involved the sale of securities as defined by the statute and alleged in the indictment."

The Court then stated that Section 2(1) of the Act:

> "[d]efines the term 'security' to include 'any note, evidence of indebtedness, investment contract, receipt for or guarantee of any such security.'"

After stating the government's contention that the various instruments offered, sold and issued in connection with the enterprise constitute and include securities within the confines of the definition above given, and the defendants' contention that such definition of securities does not include the instruments issued in the course of the offer and sale of Secured 10% Earnings, the Court stated that the jury must resolve the conflict in deciding the guilt, if any, of any of the defendants under each of such counts. The Court then stated in reference to such counts that "the requirement that the government establish that the Secured 10% Earnings offered by the defendants involved the sale of securities will be established if you find that the trust deed notes or trust deeds are 'notes' or 'evidence of indebtedness,' as defined by the Act."

In the same instruction the Court stated:

> "Regardless of whether or not you find the trust deed notes or trust deeds are 'notes' or 'evidence of indebtedness' within the applicable statute, you may find the instruments should be classified as 'investment contracts' and therefore securities within the applicable statutes."

The Court advised the jury that the term "investment contract" is not defined in the Act, but set forth certain guide lines or tests for the jury to follow in determining whether the instruments involved are "investment contracts" within the fair meaning of the statute.

Since the appellants do not question the propriety of the guide lines or tests set forth by the Court, it appears unnecessary to make further mention of them.

The Court concluded its instruction on this phase by stating to the jury:

> "If you find that the various instruments, such as trust deeds, trust deed notes, and certificates of registration and ownership, offered and sold by the defendants though not necessarily delivered to or received by certain investors, are 'notes,' 'evidence of indebtedness,' or 'investment contracts' and therefore 'securities' you may also consider and determine whether certain instruments, for example, receipts for deposits of funds issued to investors were 'receipts for' such securities and therefore themselves securities within the meaning of the statute. However, in this situation neither the definition of 'receipt for' nor 'guarantee of' a security would be applicable in the absence of a finding that an underlying security in the form of a 'note,' 'evidence of indebtedness,' or 'investment contract' had been offered or sold. You need only find that the instruments here in question constituted securities under any one of the several definitions I have given you and not all of them or more than one of them."

Appellants contend that the instruction is erroneous. Their position is set forth in the following instruction requested by them, and which the District Court refused, which requested instruction reads as follows:

> "In determining whether there was a violation of the Securities Act, you must first find that the defendants, or any one of them, engaged in the offer or sale of securities. There are a number of different types of securities. However, you will only be concerned with the type known as an 'investment contract.' If you find that the transactions charged were not investment contracts, then you must find the defendants not guilty of violation of the Securities Act in Counts One to Seventeen, inclusive."

In short, appellants contend that the trust deed notes or trust deeds offered, sold and issued by the defendants under their variously designated 10% Earnings Programs are not "notes," or "evidence of indebtedness," as defined by the Securities Act, a. l that the instruction which should have been given on the subject should have been restricted to the type of security designated in the Act as an "investment contract".

Appellants predicate their contention on the ground that the:

> "[c]ommon law characteristics of a promissory note, which might render it a 'note' within the statutory definition of a 'security', have been destroyed in California by various Legislative enactments with reference to purchase money deeds of trust. Under the successive amendments to Section 580(a), 580(b), 580(d), and Section 726 of the Code of Civil Procedure of the State of Cali-

> fornia, the maker of a purchase money deed of trust has no personal liability or obligation of any sort. The holder of the trust deed has no remedy of recourse against the maker. The trust deed becomes not an evidence of indebtness but merely evidence of a charge or lien against the land. Where there is no debt as such, there can be no evidence of indebtedness."

While we do not question the holdings of the California decisions cited by appellants in support of their interpretation of purchase money deeds of trust in California, such interpretation has no relevance in the context of the case under review.

The record reveals that the numerous investors in the Secured 10% Earnings Program were assured that they were receiving negotiable promissory notes; that their deposits with LATD&ME were like deposits in the bank; that the "estimated liquidation value" shown on their monthly statements evidenced indebtedness to them which was due and payable whenever they elected to withdraw their accounts; and that careful screening had been made as to the credit standing of the makers of the obligations. There is no evidence in the record that the investors, scattered over the United States, were informed that the makers of the obligations were shielded against liability under California law. What was represented, offered and sold to investors was not a simple purchase money trust deed note or trust deed, but a complete Secured 10% Earnings Plan or Program. To adopt appellants' interpretation would be to exalt form over substance and isolate from consideration the great mass of evidence in the record relating to the man-

ner and means employed by appellants in conducting the 10% Earnings Plan or Program. As stated by the Supreme Court in *S.E.C. v. Joiner Corporation*, 320 U.S. 344 (1943):

> "The test rather is what character the instrument is given in commerce by the terms of the offer, the plan of distribution and the economic inducements held out to the prospect. In the enforcement of an Act such as this it is not inappropriate that a promoter's offerings be judged as being what they are represented to be." (pp. 352-353).

In the context of this case, whether or not the instruments offered, issued and sold are "securities" under Federal law, *S.E.C. v. Joiner Corporation, supra; S.E.C. v. Variable Annuity Life Insurance Company of America*, 359 U.S. 65 (1959); *Los Angeles Trust Deed & Mortgage Exchange v. S.E.C.*, 264 F.2d 199 (9th Cir. 1959).

Appellants complain that the instruction fails to define the terms "any note," or "evidence of indebtedness" appearing in the statute. In our view such ordinary terms are self-defined and require no further definition. See *S.E.C. v. Joiner Corporation, supra*, p. 355.

Finally, under this assignment appellants advance the argument that this Court in *L. A. Trust Deed & Mortgage Exchange v. SEC*, *supra*, and *L. A. Trust Deed & Mortgage Exchange v. SEC*, 285 F.2d 162 (9th Cir. 1960), C.D. 366 U.S. 919, by implication has held that the instruments herein involved are not "notes" or "evidence of indebtedness" under the Act. We do not so read said decisions.

We find no error in the instruction given by the District Court, or in the rejection by the District Court of the instruction offered by appellants.

The second assignment:

> "II. The Court erred in allowing introduction of any evidence of the existence of the prior civil action or the issues involved therein and its determination. There was also error in the phrasing of the Court summary and in the Court's failing to instruct at that time the difference between the burdens of proof in the two actions."

The criminal action herein was preceded by civil litigation instituted by the S.E.C. against the corporations above named, the appellants, and others in which the Commission sought to enjoin the defendants therein named from engaging in acts and practices constituting violations of the Securities Act in offering and selling to the public trust deed notes and trust deeds under the Secured 10% Earnings Plan or Program. In supplemental or amended complaints the S.E.C. sought the appointment of a receiver and charged, *inter alia*, that the corporate defendants were misappropriating funds entrusted to their care under the Secured 10% Earnings Program and were insolvent. The District Court granted a preliminary injunction and made the appointment of a temporary receiver. This Court stayed the operation of such orders pending appeal, issued a substitute restraining order and expedited the appeal. On appeal, this Court set aside the preliminary injunction and the order appointing a temporary receiver, and the matter was remanded for a complete trial on the merits, and ordered this Court's substitute restraining order con-

tinued in full force and effect pending the trial. See 264 F.2d 199, supra.

On May 20 1960, the District Court, after full trial, appointed a receiver for two of the three named corporate defendants. See *186 F.Supp. 830 (1960)*. We interpreted the order made below as requiring a complete liquidation by the receiver of the corporate defendants. We stayed that order for complete liquidation and ordered the receiver to maintain, preserve and conserve the assets pending the determination of the appeal from the judgment below. This judgment, except as to liquidation powers of the receiver, was affirmed by this Court. See *285 F.2d 102, supra*.

In conferences between Court and counsel, in the absence of the jury, counsel for the government stated that he intended to offer into evidence pleadings and judgment of the District Court in the civil litigation, copies of which had been marked for identification. Counsel for the appellants objected. The District Court indicated that portions of such documents might be relevant and material on the question of good faith, but stated other portions, if not relevant, might be prejudicial. After further discussion and consideration, the District Court refused to receive the documents in evidence and in lieu thereof made the following statement to the jury.

> "Members of the jury, in lieu of the acceptance in evidence of Exhibits 1950, 5200, 5201 and 1950-A, I will give you a summary of some of the facts in such exhibits which I deem of possible relevance or materiality for your consideration.
>
> "On March 24, 1958, the Securities & Exchange Commission filed a Complaint against Los Angeles

Trust Deed and Mortgage Exchange, Trust Deed & Mortgage Exchange, Trust Deed & Mortgage Markets, David Farrell, Oliver J. Farrell, Roy A. Bonner, and Thomas Wolfe, Jr., charging the defendants with violation of certain Sections of the Securities Exchange Act, including charges that defendants were engaged in transactions, practices and a course of business which operated and would operate as a fraud and deceit upon purchasers of such alleged securities.

"On October 8th, 1958, the Commission filed an Amended and Supplemental Complaint charging the corporate defendants with misappropriation of funds entrusted to them by investors under the Secured 10% Earnings Program, and further charged that said corporate defendants were insolvent and unable to meet their current obligations. The Amended Complaint included as a party defendant Stanley C. Marks.

"The charges in both the original and the Amended and Supplemental Complaint were denied by the defendants.

"On May 20, 1960, a judgment was entered in said proceedings permanently enjoining the defendants from engaging in the acts as charged. The effect, however, of this injunction was stayed —that is, put off—by an appeal.

"Pursuant to the judgment the Receiver took charge of the assets and business of the corporate defendants on June 8, 1960.

"Now, neither the charges made in the pleadings in such case nor said judgment are to be considered by you as evidence of the truth of such

charges. The above statement of facts is given to you solely in connection with your consideration of the charges made in Paragraph 11, Count one, of the indictment."

Paragraph 11, Count one of the indictment, in substance alleges: That it was an element of the scheme and artifice to defraud; that the defendants, in order to deceive and mislead investors, falsely represented to investors that the Secured 10% Earnings Program constituted a legal investment plan which conformed to all applicable laws, and had been approved and evaluated by a former counsel for S.E.C., whereas, appellants concealed from, and omitted to state to investors that the S.E.C. had filed a civil litigation to restrain defendants from engaging in practices in violation of the Act, based on allegations of fraud and insolvency. It further alleged that after the civil trial defendants continued to solicit deposits without disclosing or making known to investors the nature and import of the procedures, or the fact the program might be made subject to administration in the course of a receivership.

Appellants appear to recognize the fact that the short summary of the civil litigation given by the Court to the jury was a fair statement. Clearly, the government was entitled to offer proof on the allegations contained in paragraph 11 of Count one which were alleged to constitute an element of the scheme or plan to defraud. It appears to us that the District Court acted with more caution and restraint than the circumstances required. By the method adopted by the District Court, inflammatory statements appearing in the judgment were kept from the jury. The District Court

carefully instructed the jury that the charges contained in the pleadings had been denied by the defendants, and that the summary of the civil litigation should not be considered by the jury as evidence of the truth of the charges. In view of this statement and other instructions given as to the burden of proof, we find no error on the part of the District Court.

The third assignment:

> "III. The Court erred in allowing any testimony of losses by customer witnesses in that such evidence was (a) immaterial and irrelevant to the crimes alleged and (b) violative of the Court's own ruling in reference to events occurring after June 7, 1960."

The law appears to be well settled that in a prosecution of this type, the government is not required to prove that anyone was defrauded or that any investor sustained loss. *Bobbroff v. United States*, 202 F.2d 389 (9th Cir. 1953). Such evidence, however, is not inadmissible. *Lonergan v. United States*, 95 F.2d 643 (9th Cir. 1938), C.D. 304 (U.S. 581). In *Linden v. United States*, 254 F.2d 500 (4th Cir. 1958), the Court stated at page 506:

> "Proof that the scheme was effective should not be excluded as irrelevant. While it is true that the success of a scheme is not a necessary element of the crime defined in the Mail Fraud statute, nevertheless where, as here, the indictment charges the defendant with making captious, deceptive, and misleading solicitations, the effect of the solicitations upon the recipients is a highly pertinent fact in determining whether the solicita-

tions are of the nature charged. Cf. *Silverman v. United States*, 3 Cir., 1954, 213 F.2d 405, 407; *Haid v. United States*, 9 Cir., 1946, 157 F.2d 630, 632. The tendency of the form to mislead is shown by testimony that it did mislead."

We believe, as did the District Court, that such evidence was relevant and material in establishing the quality of the trust deeds and the financial condition of LATD&ME prior to the receivership.

It was appellants' position that they should not be held responsible for losses occurring to investors after June 7, 1960, the date of the appointment of the receiver. The District Court agreed with that position and instructed the jury that:

> "The evidence in this case of a bankruptcy or a receivership of Los Angeles Trust Deed and Mortgage Exchange is not to be considered by you as evidence of the guilt of any one or more of the defendants, or evidence on any other issue in the case. You shall disregard any evidence or testimony of any customer of LATD&ME and affiliated companies to the effect that a loss was suffered after June 7, 1960. The defendants are not charged with responsibility for acts occurring after that time."

The fact that in this long and complicated trial some evidence may have gotten into the record by investor witnesses that they had not received their investments back at the time their testimony was given, does not constitute prejudicial error sufficient to warrant a re-

versal. It is to be presumed that the jury heeded the instruction of the court and that any error in the admission of such evidence was cured by the cautionary instruction given by the Court.

Appellants also claim that they were prejudiced by the fact that certain witnesses called by the government were aged, unemployed, uneducated, or widows with limited income. Such persons were named in various counts of the indictment as being persons to whom literature was sent by defendants, soliciting participation in the Secured 10% Earnings Program, and who participated therein, and who gave testimony that they had never gotten their money back. Appellants contend that such witnesses were deliberately staged by the government in order to evoke the sympathy of the jury and engender antipathy against the defendants. The record reveals that the government fairly presented a cross section of "investor" witnesses. Other witnesses who testified were a thirty-five year old real estate broker, a forty-four year old salesman, a fifty-three year old businessman, a school teacher, a novelist, and a retired businessman. No objection was made by appellants to the calling of witnesses of the class to which they now complain, although opportunity to do so was furnished in procedures which had been adopted during the pretrial conferences. We find no reversible error under this assignment.

The fourth assignment:

> "IV. The Court erred in admitting Exhibit 6003 in evidence."

Exhibit 6003 consists of approximately eight hundred customer "sell orders" together with their at-

tached covering letters, all of which were contained in two baskets. Each of the "sell orders" was basically a small sheet of yellow paper instructing LATD&ME to liquidate the customer's account. The item contained in this exhibit to which the appellants make the most strenuous objection was a clipping from a newspaper of comments made by Judge Thurmond Clarke, presiding judge in the civil litigation, which comments were derogatory of appellants' business methods, and which clipping was attached to a request for liquidation of the investor's account. Appellants also contend that many of the covering letters attached to the "sell orders" were prejudicial.

The fact that the exhibit contained the objectionable items was not called to the attention of the District Court until the hearing on appellants' motions for directed verdicts or in the alternative a new trial. Exhibit 6003 was a part of the records in possession of LATD&ME at the time that it went into receivership. At the time the exhibit was offered, the only objection made by appellants was no proper foundation had been established. It appears that for some three weeks prior to the offer of the exhibit in evidence that the exhibit was available for inspection by the appellants. There is some indication gleaned from the hearing on the motions that at least one appellant had some knowledge of the existence of the newspaper clipping before the case was submitted to the jury for determination and before the exhibit was sent to the jury room along with other exhibits. In any event, appellants had knowledge of the presence in Exhibit 6003 of the items to which they now object while the jury was still deliberating.

At the conclusion of the hearing on appellants' motions for directed verdicts or in the alternative for a new trial, the District Court stated:

"As I mentioned at the start, I had read the showing in support of the motion for a new trial by each of the defendants and for a judgment in favor of each defendant. All, or practically all of the questions raised were raised at the time of trial and raised before the matter was submitted to the jury, and therefore were matters which had been considered by the court at the time of the trial itself. However, there was the new question which was raised, or you might say new questions in connection with Exhibit 6003. Now with the explanation which we have here this morning, I feel that there was an obligation on, first of all, the part of the defendants, when the defendants knew that that particular material was in 6003; to so advise the court, and of course, there is no doubt but that the court would have removed that from the file, and if there was other material in the file of a like nature, such as letters, there is no doubt but that the court would have removed that. I think the record here speaks for itself that during the course of the trial every time a matter was mentioned where some objectionable material was on an exhibit, that the court, if it admitted it at all, admitted it provisionally on the removal of the objectionable material. So in view of that fact, and of the further fact that before the jury returned its verdict that counsel for David Farrell was informed, at least, that the exhibit might be in the possession of the jury, and that that information was not called to

the attention of the court, at which time the court might then have called for a return of the exhibits, in order to determine if the jury had in any manner investigated this particular exhibit, at that time, the court could even have interrogated each one of the jurors as to whether they had read the particular article. And maybe the court, if the jurors had said yes, why, at that time maybe the court would have declared a mistrial. But now the defendants have taken their chance, and whether the jurors or any one of the jurors read it, of course we don't know. I, therefore, feel that if there was any error committed in permitting this or the other exhibits containing, say, like material if there are such, why, that error was at least in part invited by the defendants and that they should not at this time be permitted to claim that it should not have happened."

We find ourselves in agreement with the views expressed by the District Court, and hold that the error, if any, in the admission into evidence of the exhibit does not warrant reversal.

Appellants' final contention in connection with this assignment is that Exhibit 6002 which was received in evidence as a summary of Exhibit 6003 was not a true summary of Exhibit 6003, in that it did not contain a complete summary but was only a synopsis of the requests for liquidation which were on hand on June 8, 1960. The summary listed the customer's number, the date of request and the amount that was requested for liquidation. The aggregate amount requested for liquidation was $3,600,000.00. The summary was exactly what it purported to be, and the fact that it may not

have contained other information does not render it admissible as a summary.

From our study of the record in this case, we find that none of the errors assigned warrants a reversal of the judgment of conviction. The trial was a protracted and a complicated one. The District Judge presided over the trial with ability, fairness, impartiality, and was ever alert to protect the substantial rights of the appellants. In our judgment the appellants received a fair trial.

The judgments of conviction are affirmed.

(Endorsed) Opinion Filed Aug. 7, 1963.

Frank H. Schmid, Clerk.

APPENDIX II.

Judgment and Commitment.

United States District Court, Southern District of California, Central Division.

United States of America v. David Farrell. No. 30,341—Criminal.

On this 14th day of May, 1962 came the attorney for the government and the defendant appeared in person and with his counsel, Lloyd F. Dunn.

It Is Adjudged that the defendant has been convicted upon his plea of not guilty, and a verdict of guilty of the offense of violating Title 15, United States Code, Section 77q(a)(1) and Section 17(a)(1), Securities Act of 1933 as charged in Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17 of the Indictment; and, of violating Title 18, United States Code, Section 1341 as charged in Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 of the Indictment; and of violating Title 18, United States Code, Section 371 as charged in Count 34 of the Indictment and the Court having asked the defendant whether he has anything to say why judgment should not be pronounced, and no sufficient cause to the contrary being shown or appearing to the Court.

It Is Adjudged that the defendant is guilty as charged and convicted.

It Is Adjudged that the defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of five (5) years and fined the sum of $4,000.00 on Count One.

It Is Further Adjudged that defendant be committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of five (5) years and fined the sum of $4,000.00 on each of Counts 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17; and that prison sentences on each and all of said Counts begin and run concurrently and begin and run concurrently with Count One making a total imprisonment of five (5) years and a total fine of $64,000.00.

It Is Further Adjudged that defendant is hereby committed to the custody of the Attorney General or his duly authorized representative for a period of five years on Count 18 and fined the sum of $1,000.00 on said Count.

It Is Further Adjudged that defendant is committed to the custody of the Attorney General or his duly authorized representative for a period of five years and fined the sum of $1,000.00 on each of Counts 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32; and that prison sentences on each and all of said Counts begin and run concurrently and begin and run concurrently with Count 18 making a total imprisonment of five (5) years and a total fine of $15,000.00.

It Is Further Adjudged that defendant be committed to the custody of the Attorney General or his duly authorized representative for a period of five (5) years and fined the sum of $7,500.00 on Count 34.

It Is Further Adjudged that the prison sentences under Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 begin and run concurrently with the prison sentences under Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17; and that the prison sen-

tence under Count 34 begin and run concurrently with the prison sentences under Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17 and that the prison sentence under Count 34 begin and run Consecutively with the prison sentences under Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 making a total of ten (10) years imprisonment to be served by the defendant and a total of $86,500.00 in fines to be paid by defendant.

It Is Further Adjudged that, in light of the defendant's war record and his former reputation and standing in the community in which he lived, the provisions of Title 18, United States Code, Section 4208(a) are hereby invoked and the above prison sentence of ten (10) years is fixed as the maximum and the defendant shall become eligible for parole at such time as the U. S. Board of Parole may determine.

It Is Further Adjudged that execution of sentence be stayed until 4:30 PM, May 16, 1962, and that in the event bail on appeal is posted then the execution of the fines herein levied is stayed pending appeal.

It Is Further Adjudged that upon posting of bail on appeal, Court Appearance bond of the defendant shall be exonerated.

It Is Ordered that bail on appeal is set in the amount of Fifty Thousand Dollars ($50,000.00).

It Is Ordered that the Clerk deliver a certified copy of this judgment and commitment to the United States

Marshal or other qualified officer and that the copy serve as the commitment of the defendant.

JOHN F. KILKENNY
United States District Judge

Filed: May 14, 1962
John A. Childress, Clerk
by L. A. BROSNAN,
Deputy Clerk

Approved as to Form:

[Illegible]
Assistant U. S. Attorney

Judgment and Commitment.

United States District Court, Southern District of California, Central Division.

United States of America v. Oliver J. Farrell. No. 30,341—Criminal.

On this 14th day of May, 1962 came the attorney for the government and the defendant appeared in person and with his counsel Eugene L. Holder.

It Is Adjudged that the defendant has been convicted upon his plea of not guilty, and a verdict of guilty of the offense of violating Title 15, United States Code, Section 77q(a)(1) and Section 17(a)(1), Securities Act of 1933 as charged in Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17 of the Indictment; and, of violating Title 18, United States Code, Section 1341 as charged in Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 of the Indictment; and, of violating Title 18, United States Code, Section 371 as charged in Count 34 of the Indictment and the Court having asked the defendant whether he has anything to say why judgment should not be pronounced, and no sufficient cause to the contrary being shown or appearing to the Court,

It Is Adjudged that the defendant is guilty as charged and convicted.

It Is Adjudged that the defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of two (2) years and fined the sum of $2,000.00 on Count 1.

It Is Further Adjudged that the defendant is hereby committed to the custody of the Attorney General or

his authorized representative for imprisonment for a period of two (2) years and fined the sum of $2,000.00 on each of Counts 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17; and that prison sentences on each and all of said Counts begin and run concurrently and begin and run concurrently with Count 1 making a total imprisonment of two (2) years and a total fine of $32,000.00 on said Counts.

It Is Further Adjudged that defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of two (2) years and fined the sum of $1,000.00 on Count 18.

It Is Further Adjudged that defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of two (2) years and fined the sum of $1,000.00 on each of Counts 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32; and that prison sentences on each and all of said Counts begin and run concurrently and begin and run concurrently with Count 18 making a total imprisonment of two (2) years and a total fine of $15,000.00 on said Counts.

It Is Further Adjudged that defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of two (2) years and fined the sum of $5,000.00 on Count 34.

It Is Further Adjudged that the prison sentences under Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27,

28, 29, 30, 31, and 32 begin and run concurrently with the prison sentences under Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17; and that the prison sentence under Count 34 begin and run concurrently with the prison sentences under Counts 1, 2, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, and 17 and that the prison sentence under Count 34 begin and run Consecutively with the prison sentences under Counts 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 making a total of four (4) years imprisonment to be served by the defendant and a total of $52,000.00 in fines to be paid by the defendant.

It Is Further Adjudged that the provisions of Title 18, United States Code, Section 4208(a) are hereby invoked and the above prison sentence of four (4) years is fixed as the maximum and the defendant shall become eligible for parole at such time as the U. S. Board of Parole may determine.

It Is Further Adjudged that execution of sentence be stayed until 4:30 PM, May 16, 1962 and that in the event bail on appeal is posted then the execution of the payment of the fines herein levied is stayed pending appeal.

It Is Further Adjudged that upon posting of bail on appeal, Court Appearance bond of the defendant shall be exonerated.

It Is Ordered that bail on appeal is set in the amount of Twenty Thousand Dollars ($20,000.00).

It Is Ordered that the Clerk deliver a certified copy of this judgment and commitment to the United States Marshal or other qualified officer and that the copy serve as the commitment of the defendant.

JOHN F. KILKENNY.
United States District Judge.
By L. A. BROSNAN.
L. A. Brosnan Deputy Clerk.

Filed: May 14, 1962.
JOHN A. CHILDRESS, Clerk.

Approved as to Form:
[Illegible]
Assistant U. S. Attorney

APPENDIX III.

[Court's Instructions re: Securities—R. T. 4266-4274.]

* * * * *

"Counts Three and Thirty-three of the indictment have been dismissed and are no longer subject to your consideration. Counts One and Two and Counts Four through Seventeen of the indictment each alleges that the defendants devised and executed a scheme to defraud in the sale of "securities" as defined in Section 2(1) of the Securities Act of 1933, namely, "investment contracts, promissory notes, evidence of indebtedness and receipts for and guarantees of such securities," in connection with an investment plan, program and arrangement designated by the defendants as a Secured 10% Earnings Program, Secured 10% Earnings Reinvestment Program, Secured 10% Earnings Accounts, and other similar designations, based on the sale to members of the investing public of discounted trust deeds and mort-[4266] gages, in violation of Section 17(a)(1) of the Act, making it unlawful "for any person to offer for sale any securities, by the use of any means or instruments of transportation or communication in interstate commerce, or by use of the mails, directly or indirectly, to employ any device, scheme or artifice to defraud."

Therefore, in order to sustain all or any one of these counts; that is, the counts under the Securities Act, it is essential that you find not only that the defendants devised and engaged in a scheme to defraud by use of the mails, as alleged in the indictment, but also that the scheme to defraud involved the sale of securities as defined by the statute and alleged in the indictment.

Section 2(1) of the Act defines the term "security" to include "any note, evidence of indebtedness, investment contract, receipt for or guarantee" of any such security.

The government contends that the various instruments offered, sold and issued in connection with the defendants' enterprise constitute and include securities within the confines of that definition.

The defendants contend that said definition of securities does not include the instruments issued in the course of the offer and sale of Secured 10% Earnings. This is a question which you must resolve in deciding the guilt, if any, of the defendants under each of the counts above [4267] mentioned. Counts Eighteen to Thirty-two, inclusive, of the indictment allege offenses under the Mail Fraud Statutes, and it is not a necessary element to the crime of mail fraud under such statutes that the scheme to defraud involve the sale of securities.

Going back to the charges under the Securities Act, the requirement that the government establish that the Secured 10% Earnings offered by the defendants involved the sale of securities will be established if you find that the trust deed notes or trust deeds are "notes" or "evidence of indebtedness," as defined by the Act.

Regardless of whether or not you find the trust deed notes or trust deeds are "notes" or "evidence of indebtedness" within the applicable statute, you may find the instruments should be classified as "investment contracts" and therefore securities within the applicable statutes.

The term "investment contract" is not defined in the Act. There are, however, certain guide lines for you to follow in determining, in light of the dominating general purpose of the statute to protect the investing public, whether the instruments are "investment contracts" within the fair meaning of the statute. A basic test is "what character the investment is given in commerce by the terms of the offer, the plan of distribution, and the economic in-[4268]ducements held out to those who are solicited to invest." You may take into account, for example, the fact that the defendants themselves, at times, have used the term "investment securities" and "security" in referring to Secured 10% Earnings and have used the designation "Investor's Ledger" in their internal accounting system. In this connection it is necessary that you give consideration to the basic and essential nature of the enterprise and to all surrounding and collateral facts and circumstances, including the representations and inducements, if any, both written and verbal, held out to investors whose funds the defendants solicited and obtained. You may consider the entire fabric of the enterprise in the light of the disclosures made by the defendants and those not made by them, if any, in order to determine whether, either with or without the knowledge of investors whose funds were committed to the defendants for investment, there existed among them a "community of interest" and whether the economic welfare of those investors was interwoven with the ability of Los Angeles Trust Deed & Mortgage Exchange to make good whatever representations, commitments and promises were made to investors by or at the instance of the defendants, such as, for example,

to accomplish the liquidation of investors' accounts at "estimated liquidation values."

In determining whether the instruments offered and [4269] sold were "investment contracts," you may consider whether investors were led to expect Secured 10% Earnings solely on the basis of the ability of the defendants to select, screen, appraise and acquire trust deeds suitable for Secured 10% Earnings and the continuous reinvestment of accounts to yield earnings at 10% per annum compounded monthly, to service and collect trust deeds sold to investors and, if necessary, to carry out foreclosure proceedings on behalf of investors. You may also take into account the fact that the evidence shows that many of the investors reside in states and foreign countries outside the State of California where the lands securing the trust deeds were situated.

You may also take into account evidence establishing the extent which, if at all, the defendants may have created a situation where they possessed or exercised dominion or control over the accounts of investors, and introduced trust deeds into the accounts or to withdraw such trust deeds. The circumstances under which trust deeds were created, brought into inventory and introduced into the accounts of investors, the nature and quality of the trust deeds, their economic value as separate units, the likelihood that investors might be required to engage in concerted action to enforce their rights in the event of default by the trustors, and the extent to which the investors may have been led to look to the defendants to pro-[4270]tect and enforce their rights are elements for your consideration in de-

termining whether the instruments offered were "investment contracts" within the meaning of the statute.

If, under all of the evidence, you find that the defendants created a condition under which a "community of interest" existed among investors; that is, a condition under which the economic welfare of investors was dependent upon the solvency, financial stability, resources and liquidity of LATD&ME — I think you are now familiar with those initials — and its affiliates and subsidiaries, and that investors were led to expect Secured 10% Earnings solely from the efforts of the defendants, after giving due consideration to all elements of the offering, then, as a matter of law, the instruments offered and sold were "investment contracts" and therefore securities within the meaning of the Federal Securities Act.

If you find that the various instruments, such as trust deeds trust deed notes, and certificates of registration and ownership, offered and sold by the defendants though not necessarily delivered to or received by certain investors, are "notes," "evidence of indebtedness," or "investment contracts" and therefore "securities," you may also consider and determine whether certain instruments, for example, receipts for deposits of funds issued to investors were "receipts for" such securities and therefore themselves [427] securities within the meaning of the statute. However, in this situation neither the definition of "receipt for" nor "guarantee of" a security would be applicable in the absence of a finding that an underlying security in the form of a "note", "evidence of indebtedness," or "investment contract" had been offered or sold. You need only find that the instruments here in question constituted

securities under any one of the several definitions I have given you and not all of them or more than one of them:

Counts Eighteen through Thirty-two of the indictment charge the defendants with violation of the Mail Fraud Statute, 18 USC 1341. The Mail Fraud Statute, as far as material to this case, provides:

> "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations or promises . . . for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department, or takes or receives therefrom any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at the place at which it is directed to [4272] be delivered by the person to whom it is addressed, any such matter or thing, shall be"

punished as provided for in such statute.

You will note that the Mail Fraud Statute and Section 17(a)(1) of the Securities Act of 1933 are quite similar. Each makes it unlawful to employ a scheme or artifice to defraud through deceit and misrepresentation when the mails are used. However, the coverage of the two laws is not the same. As I have previously explained, Section 17(a)(1) of the Securities Act applies only where the scheme to defraud involves the offer or sale of securities. The Mail Fraud Statute has no such requirement.

On each of the counts brought under the Securities Act of 1933, the government must prove beyond a reasonable doubt the following:

(1) That the documents in question were "securities" within the meaning of the law;

(2) That there was a scheme or artifice to defraud the named investors out of money of [sic] property by means of false or fraudulent representations;

(3) That defendants participated in the scheme, if any, with knowledge of its fraudulent character, if any; and

(4) That one or more of defendants were participants in the alleged scheme to defraud and that the specific [4273] acts of mailing, as alleged, have been proved to have been done in the execution of the alleged scheme.

The last three requirements apply to each and all of the remaining counts in the indictment brought under the Mail Fraud Statute. In other words, the Government must prove beyond a reasonable doubt on each of said Securities Act and Mail Fraud counts:

First, that one or more of the defendants named therein devised a scheme and artifice to obtain money by false and fraudulent representations as alleged in each count;

Second, that for the purposes of carrying out such scheme one or more of defendants, within the State and District of California, did on or about the date mentioned in each count knowingly, unlawfully and willfully cause to be placed into an authorized depository for United States mail an envelope containing mail matter and addressed as therein alleged, within said District of California;

Third, that defendants so used the United States mails willfully and with specific intent and purpose of executing or carrying out said scheme or artifice to defraud, if any, and on the alleged Securities Act violations that the documents were securities as defined in the Act. [4274]."

* * * * *

APPENDIX IV.

[R. 1088]:

"Mr. Dunn: It was my understanding from that that we would not go into matters after June 8, 1960. However, they were gone into. It got into the record as it stood, and we would like to reserve our rights and make any proper motion to strike. But at this time I would like to also move that the Government be instructed not to attempt to present matters regarding defaults and what occurred to the property after June 8, 1960, when the receiver was in control of Los Angeles Trust Deed & Mortgage Exchange.

That would be a general motion, because I assume—

* * *

"The Court: . . . .

Now, I would like to just hear from the Government as to how you believe that that can have any relevancy or materiality whatsoever. After all, if there was an insolvency on the date of the receivership, that is it. If something else was caused or happened after that time, what difference does it make?

Mr. Medvene: If the court please, that wouldn't have anything to do with the insolvency. What the testimony would have to do with, your Honor, is whether in truth or in fact the trust deeds were actually prime, trouble-free, well-screened trust deeds. And we think the evidence that the trust deeds were delinquent—not because of any condition necessarily of LATD, but were delinquent because of the nature or type of property that they

were put on, and that this had relevance in relationship to the program as it was presented to the potential investor.

The Court: The ultimate question, though, would be the nature of the trust deeds as of the date of receivership rather than what happened later, Mr. Medvene, because I think we all have to recognize that the appointment of a receiver is necessarily going to affect the value of whatever the security might be, if they had anything to do with it. *So I really think that our basic problem is what were the values as of the date of the receivership and before that time.*" (Emphasis added.)

* * *

[Continuing R. 1092]

"The Court: I am still going to hold my reservation of ruling on it. I think Mr. Medvene, you may be getting into dangerous territory.

* * *

The Court: I will still reserve my ruling and let us keep away from that during the course of the day here, and I will think about it over the week-end and we will have a ruling on Monday.

* * *

[which the Court did R. 1293]:

"The Court: All right.

With reference to the general line of testimony that is before and after the receivership, gentlemen, I don't believe at this time, at least, that I can adopt a general rule on that. I believe that under some circumstances such evidence is admis-

sible, such as *United States vs. Tellier*, 255 F. 2d 440, 448, 449. In other cases it has been held inadmissible. And the reason for the distinction between the two becomes obvious to anyone who would read the cases.

So for that reason I feel that I cannot adopt a general rule on it, although to say this: *That generally speaking what happened after that time, except insofar as it might be declarations against interest, or something such as that, why, it would seem to be inadmissible, or that it wouldn't have any particular relevancy or materiality . . .*" (Emphasis added.)

[R. 1479-1481]:

". . . it would seem to me that a great deal of time could be saved by just asking the witnesses direct questions as to the amount of money they put in and under what circumstances they put it in *and whether they ever got it out*, and the type of trust deeds . . . (Emphasis added.)

* * *

[R. 1516]:

"The Court: . . . If you want to ask him if he got the money back. . . .

Q. By Mr. Schulman: Did you receive your investment back from the Los Angeles Trust Deed & Mortgage Exchange, sir?

Mr. Jacobs: I object to that for the reason, your Honor, it would be a question of whether he received his funds as represented prior to June 7, 1960.

The Court: This might be some evidence of the condition of the company at the time. The objection is overruled.

Did you receive your money back? Answer the question Yes or No. That is the question. As I say, I think you have already answered it, but answer it again for counsel.

The Witness: No, I only received a small part of it back.

Q. By Mr. Schulman: Did you receive a full-term 10% return on your earnings, sir? A. While it was invested in the company up to this date that you mentioned, yes, I did. Since then, no."

[R. 1517]:

"By Mr. Jacobs: Q. You made a remark, sir, that you had sustained certain losses. The fact is that any loss you sustained, or I assume you have sustained, was subsequent to the time that the receiver took over the Mortgage Company; isn't that correct?

Mr. Schulman: An objection, your Honor. This is the same conclusion that I believe Mr. Jacobs objected to before.

The Court: I will sustain the objection."

This ruling was discussed later [R. 1540-42] and the Court said:

"The Court:

"What I am attempting to hold it to here is that I believe the Government has a right to show that these people did not get all their money back, and that the particular witness has a right to express his opinion, since he is the owner of the property.

after looking back on it as to the value and as to whether it was valueless or whether it was not. That is the position of the court at the present time, and I am trying to hold it to that June 7th date.

* * *

I think we all recognize—certainly I do—that even though it might be a prime second trust deed, the fact that insolvency occurred of some kind and that that paper was still in the possession of the company might affect the market value of that second trust deed.

* * *

The Court: I recognize that, but I will stay with my original cutoff date there, the date of the receivership. It is the values as of that date, and although information might have been obtained later, it would be the values as of that date. I will stay with those rulings.

[R. 1847]:

"The Court: No, counsel. You may ask *if he tried* to get it back and *when*, and then you will keep within the rule on it." (Emphasis added.)

[R. 4304]:

"The evidence in this case of a bankruptcy or a receivership of LATD&ME is not to be considered by you as evidence of the guilt of any one or more of the defendants or evidence on any other issue in the case.

You shall disregard any evidence or testimony of Los Angeles Trust Deed & Mortgage Exchange and affiliated companies to the effect that a loss was suffered after June 7, 1960. The defendants

are not charged with responsibility for acts occurring after that date."

EPPLEY [R. 775]:

"Q. *Did* you *ever* receive that money, Mrs. Eppley? (Emphasis added.) A. No I *haven't*." (Emphasis added.)

MARTENS [R. 1017]:

"Q. *Did you ever get back* your money from Los Angeles Trust Deed & Mortgage Exchange? (Emphasis added.) A. No, sir; I didn't; not one dime."

BROOME [R. 1126]:

"Q. *Have you ever received* any or all of the money which you paid into or deposited with Los Angeles Trust Deed & Mortgage Exchange back from the company, sir? (Emphasis added.) A. Any or all?

Q. Any part or all of the monies which you invested with the company, *did* you ever receive it back? (Emphasis added.) A. I never received a cent back from the company . . ."

HEXNO [R. 1147]:

"Q. Did you ever receive all or any portion of your $1,000 deposit back from L. A. Trust Deed? A. No.

Q. Did you ever receive any part of any earnings back from L. A. Trust Deed? A. No."

FREEDMAN [R. 1499-1500]:

"Q. By Mr. Schulman: . . . 'we have charged your account $3,470.86.' did you ever receive that $3,470.86 back from this investment? A. No, I lost it.

* * *

[R. 1506]:

"Q. Did you ever receive your money out of this trust deed investment, sir? A. No, I lost it.

* * *

[R. 1508]:

"Q. Sir, the cash to you on this was $1,582.52. Did you receive the full amount of your investment back? A. No. I suffered a partial loss.

* * *

[R. 1511]:

"Q. The cash to you on this of or, for $601.35. did you ever get back that investment or any part of it, sir? A. Not *as yet*. (Emphasis added.)

* * *

[R. 1516]:

"The Court: . . .

If you want to ask him if he got the money back—I think you have already asked him.

Q. By Mr. Schulman: Did you receive your investment back from Los Angeles Trust Deed & Mortgage Exchange, sir?

Mr. Jacobs: I object to that for the reason, your Honor, it would be a question of whether he received his funds as represented prior to June 7, 1960.

The Court: This might be some evidence of the condition of the company at the time. The objection is overruled.

The Court: Did you receive your money back? Answer the question Yes or No. That is the question. As I say, I think you have already answered it. But answer it again for counsel.

The Witness: No, I only received a small part of it back.

Q. By Mr. Schulman: Did you receive a full-term 10% return on your earnings, sir? A. While it was invested in the company up to this date that you mentioned, yes, I did. Since then no."

HLAVKA [R. 1802]:

"Q. . . . Referring to the $1,000 on that receipt that you are holding in your hand, and any other monies that were indicated on the condensed summaries which you received monthly, have you ever received any of that back? A. No, I didn't. . . ."

LEES [R. 1831]:

"Q. How much of that ten thousand three hundred thirty-six odd dollar figure have you ever received back from Los Angeles Trust Deed & Mortgage? A. Nothing."

YOUNGS [R. 1840]:

"Q. Have you ever gotten a cent back, Mr. Youngs? A. No, sir."

CAMPBELL [R. 1856]:

"Q. By Mr. Schulman: Relating to this amount on this May 31st, did you ever receive that amount of money or any other amount of money back from L. A. Trust Deed? A. Not a cent."

SCHANZ [R. 1877 *et seq.*]:

"Q. Mr. Schanz, did you ever receive a penny back on this trust deed?

Mr. Jacobs: I object to that, if the court please.

There is no foundation laid for it from a time standpoint or whether any demand was made.

The Court: Ask him the question if he ever asked for any of it back.

The Witness: No, I never got any money back.

Q. By Mr. Medvene: Have you ever gotten anything back on it? A. No I haven't.

Mr. Jacobs: I don't think the question that was referred to, your Honor, that we were talking about was asked him. I didn't hear it.

The Court: Did he ever ask for anything back?

Mr. Medvene: *He never asked prior to the receiver.*

The Court: Would you ask him the question if he ever asked for it back.

Q. By Mr. Medvene: "*Did* you *ever* ask for anything back prior to the receiver. A. No, I never did.

Q. "*Have* you *ever* gotten anything back on this *note*? A. No."

LIST [R. 1905]:

"Q. *Have* you *received* all of that money back *yet*, sir? A. I received papers—

Mr. Jacobs: Just a moment.

The Court: Did you receive the money back is the question.

The Witness: No, I didn't."

DAVIS [R. 1967-8]:

"Q. *Did* you *ever* get a cent out of this? A. No."

COOK [R. 1980-81]:

"Q. *Have* you *ever* gotten a cent back from this investment? A. None whatsoever.

* * *

Q. *Have* you *ever* gotten a cent back on this property? A. Nothing at all.

* * *

Q. By Mr. Medvene: *Did* you *ever* get anything back on this? A. Nothing at all."

WEGNER [R. 1996-97]:

"Q. *Have* you *ever* received a cent back on this investment? A. No sir."

PEARSON [R. 2023]:

"Q. *Did* you *ever* get back your $28,000, sir, from the company? A. No, sir."

LIBBY [R. 2182]:

"Q. I am referring now to after you made your last deposit, the last $1,547. A. Yes.

Q. Did you receive any of your principal back from the company? A. No."

LEHMBERG [R. 2280]:

"Q. *Did* you *ever* get that money back from the company? A. None of it."

BILLINGSLEY [R. 2762]:

"Q. *Have* you *ever* received any of your principal back from the company? A. I have not."

APPENDIX V.

The Court charged [R. 4266, 4267 and 4269] as follows:

". . . Counts One and Two and Counts Four through Seventeen of the indictment each alleges that the defendants devised and executed a scheme to defraud in the sale of 'securities' as defined in Section 2(1) of the Securities Act of 1933, namely, 'investment contracts, promissory notes, evidence of indebtedness and receipts for and guarantees of such securities' . . .

* * *

". . . Section 2(1) of the Act defines the term 'security' to include 'any note, evidence of indebtedness, investment contract, receipt for or guarantee of any such security.

* * *

"Going back to the charges under the Securities Act, the requirement that the government establish that the Secured 10% Earnings offered by the defendants involved the sale of securities will be established if you find that the trust deed notes or trust deeds are 'notes' or 'evidence of indebtedness,' as defined by the Act."

Appellant objected to this charge [R. 4311-4312] as follows:

"Mr. Dunn: With reference to the Court's instructions as to the term 'security,' specifically since the court has included notes, I would like to call attention to the fact that notes are not within the accepted application of the statute. Although I know that the terms are that broad, they have

not been applied that broadly. They have been confined to an investment contract, as I had urged the court at the beginning. I think that we might have avoided that trouble—"

The Court: That is true. But the government would not take that position, and since the government has taken this position, I think, Mr. Dunn, since the definition is as it is, I am going to follow it.

Mr. Dunn: I have my exception, then, your Honor, that without referring to the exemptions which might apply, this is an erroneous instruction."

Appellant also asked that the Court instruct that the only type of security involved was that known as an "investment contract" [Clk. Tr. 487]:

"In determining whether there was a violation of the Securities Act you must first find that the Defendants, or any one of them, engaged in the offer or sale of securities.

There are a number of different types of securities, however, you will only be concerned with the type known as an investment contract.

If you find that the transactions charged were not investment contracts, then you must find the Defendants not guilty of violations of the Securities Act in Counts One to Seventeen, inclusive."